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C O N F I D E N T I A L SECTION 01 OF 03 DUBAI 000516

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CLASSIFIED BY: Justin Siberell, Consul General.
REASON: 1.4 (b), (d)
This message drafted jointly by Consulate General Dubai and Embassy Abu Dhabi

¶1. (C) SUMMARY: Dubai and Abu Dhabi financial markets plunged in Monday and Tuesday trading, the first market openings since Dubai World's announcement of six month moratorium on debt repayments (ref A). A senior Dubai finance official distanced the Dubai government from Dubai World's non-sovereign debt in the clearest sign to date that Dubai World, as well as Dubai's other government-related entities (GREs) cannot expect a government bailout, local or federal. In response, Dubai World executives announced the company is in direct contact with creditors. The banking sector appears to be faring better than expected, and the impact on Abu Dhabi may be less than initially believed. END SUMMARY.

UAE STOCKS DOWN SHARPLY AT MARKET OPENING

¶2. (C) UAE stocks plunged on November 30, the first day of trading since the Dubai World debt announcement, and there were additional losses in December 1 trading. The Dubai market index lost 7.3 percent and Abu Dhabi was down 8.3 percent on the 30th, for a one day loss of over USD 10 billion in market capitalization. Banks and real estate firms' clocked large losses on UAE exchanges, as was widely expected, but investors dumped everything from telecom giant Etisalat (down 9.7 percent) to the start-up Air Arabia (down 9.6 percent). Brokers complained in media reports that there were no buyers in the market, and analysts noted most investors would have sold at even lower prices if buyers could be found. It was however difficult to judge the broader regional impact of the crisis since some of the GCC markets remain closed for the Islamic Eid holiday, most notably Saudi Arabia. The reopening of Saudi Arabian exchange, which is the largest in the Gulf by market capitalization, on December 5, will provide a better idea of the possible spillover effect of the Dubai World debt announcement.

CLARIFICATIONS CONTINUE

¶3. (C) A statement by Dubai World early morning December 1st that the company is in direct talks with creditors seems to have contributed to the improvement in global markets. Dubai World characterized its discussions with creditors as "constructive" towards restructuring at least USD 26 billion of its debts, which include USD 6 billion from beleaguered Palm Island developer Nakheel. Prior to the crisis, DP World CEO Sultan bin Sulayim told Consul General that while DP World's debt load was considerable, he was confident that creditor banks would be willing to refinance to extend maturity dates given that DP World loans were backed by assets, including substantial amounts of Dubai property. Part of the DP World restructuring will include sales of DP World assets outside the UAE, albeit at considerable loss. If managed correctly, the refinance discussions with creditors and sales of assets may be the conglomerate's best effort yet to begin to meet its considerable 2009-2011 debt obligations. Also, fixed income analysts assert that the USD 4 billion in Sukuk bonds owned by Nakheel are also implicitly backed by assets consisting of the lease hold interest in all lands, buildings and other property known as DWF South and Crescent Lands at Dubai Waterfront, which could be up for grabs.

NO GURANTEES FOR DUBAI WORLD SAY AUTHORITIES

¶4. (C) In an important statement Monday, Dubai Finance Department Director General Abdul Rahman Al Saleh declared the Dubai Government's distinction between sovereign and private or corporate debt. In comments to the press, Saleh asserted that "sovereign debt is covered by a sovereign guarantee, while commercial debt is like a loan taken by any commercial entity in the market and is not guaranteed." Saleh further declared that investors bear responsibility for assuming government guarantees for DP World where none were in fact guaranteed. "It is not correct to assume that Dubai World is part of the Government of Dubai. The lenders should bear part of the responsibility," he said. The statement corroborates what Treasury Attachi heard from senior UAE Central Bank sources over the weekend wherein Abu Dhabi would back Dubai sovereign debt but not defend "private" debt built up by Dubai GRE's over the past several years. And while market participants are beginning to digest these assertions, they go against a widely-held expectation that either the Dubai or Abu Dhabi governments would ultimately back Dubai GRE obligations. The fact that they won't is a severe blow to the credibility of the Dubai-based companies that led development here and will make it very difficult for such companies to raise financing for the foreseeable future. Chief Economist at National Bank of Abu Dhabi, Giyas Gokkent, told Econ Chief that no Dubai-based entity will be able to access credit markets in the foreseeable future.

DUBAI'S GLOBAL BRAND AT RISK

¶5. (C) Despite calls from Dubai government officials that Dubai Sovereign not be too closely tied to the default of Dubai World, some participants in the bond market remain convinced that both remain inextricably linked. Dubai's brand may be tarnished for the foreseeable future despite the government's best efforts to reshape the argument about sovereign versus private debt. Sharif Eid, a bond specialist and Asset Manager at Dubai based Algebra Capital, told econoff that in the short-term, Dubai sovereign and private companies have a real black stain in the debt markets and should only expect to pay very high spreads for future bond offers. The news about Dubai World's perceived default has sullied its global brand, especially as a market leader in the Gulf and MENA region, according to Eid.

DUBAI'S DEBT ANNOUCEMENT POORLY MANAGED

¶6. (C) The market has generally viewed Dubai government's handling of the Dubai World announcement as a sign of its continued lack of transparency. A bond analyst from EFG Hermes noted to econoff that although senior Dubai government and Dubai Inc. officials continue to spin the announcement as something that was planned and anticipated, Dubai officials have unwittingly created a real credibility gap in the eyes of investors. Sheikh Ahmed Bin Saeed Al-Maktoum, who chairs the Supreme Fiscal Committee in charge of apportioning financial support to ailing companies, said last week that the Dubai Government had "full knowledge of how the markets would react" and would provide more information soon after the Islamic Eid Al Adha holiday. The UAE begins two more days of holidays associated with UAE National Day on December 2. We do not expect further clarity from senior Dubai officials until after the country returns to work December 6.

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BANKING SECTOR DOWN, BUT NOT OUT - THE VIEW FROM ABU DHABI

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¶7. (C/NF) Initial concerns about the ability of the UAE banking sector to withstand the crisis may prove to be exaggerated.

Gokkent told EconOff on December 1 that most UAE banks improved their liquid positions significantly in the past year and have applied increasingly prudent lending practices. However, even government-related banks were caught off guard by the Dubai World announcement. The economist said NBAD - the largest bank in Abu Dhabi and second largest in the UAE - always predicted Dubai would ultimately repay its debts. (Note: NBAD announced on November 30 its total Dubai World exposure (to Nakheel and Limitless) is less than USD 350 million. End Note.) While Standard and Poor's placed Abu Dhabi Commercial Bank on credit watch on November 30, it is unlikely the Abu Dhabi Investment Council, which owns over 60 percent of the bank, will let it fail. Several Dubai banks reportedly took advantage of Central Bank liquidity provisions announced in 2008 in the fall of 2009 to shore up their balance sheets. The Central Bank's new liquidity provision is also available, although the decision seems to be more of a cosmetic effort to prevent a bank run that did not materialize than a necessary step at this point.

¶8. (CN/F) Despite the Abu Dhabi market drop, Abu Dhabi's financial position appears to remain comfortable. Standard and Poor's reaffirmed Abu Dhabi's strong AA/A-1+ credit rating on November 25. While ahead of Dubai's standstill announcement, the emirate and its government related entities (GREs) remain well positioned to ride out the storm. Oil, which contributes over 60 percent of Abu Dhabi's GDP, remains priced at a comfortable USD 75 or higher. Abu Dhabi and several of its large GREs (e.g., investment firm Mubadala and developer Aldar), successfully issued over USD 7 billion in bonds over the summer (Ref B). Abu Dhabi's fiscal and trade position remain strong, likely encouraging investors to continue to view it on par with Qatar, rather than Dubai. Despite its relative strength, there is still much about Dubai's situation that likely concerns Abu Dhabi officials, as the government, private sector, and individual citizens still hold significant investments in Dubai, particularly in real estate.

COMMENT

¶9. (C/NF) While many in the UAE had hoped that the worst of the economic crisis was behind them, reality is beginning to set in that 2010 may actually be worse than 2009. Real estate and other asset prices will likely continue to decline, particularly in Dubai, which already witnessed real estate declines of over 40 percent in some areas. Dubai Government spending may contract, as trade volumes, tourism and financial sector also continue to weaken in the coming months. While it is now clear that there is no government bail-out for Dubai World, some form of support from Abu Dhabi is likely still in the cards, particularly if GCC markets see similar declines to UAE markets and fears of a significant regional impact materialize. END COMMENT
SIBERELL